

## Internal Revenue Service

Department of the Treasury  
Washington, DC 20224

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Person To Contact:

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Date:

July 9, 2014

### Legend

Administrator	=
Municipal Code	=
City	=
City Council	=
Department 1	=
Department 2	=
Retirement	=
Board	
State	=
Sub-Trust 1	=
Sub-Trust 2	=
Trust	=
Date 1	=
Date 2	=

Dear :

This letter responds to a letter from your authorized representative dated January 27, 2014, requesting a ruling that the Trust's income is excludable from gross income under Internal Revenue Code ("IRC") § 115. The Trust represents the facts as follows.

### FACTS

The City is a political subdivision of the State. The City provides health and welfare benefits to retirees and dependents of the Department 1 and the Department 2 pursuant to the terms of various health plans approved by the City Council. The City established

the Trust to provide a funding source for the payment of its liabilities pursuant to the health plans. The Trust consists of two sub-trusts. The Sub-Trust 1 will be used for the sole and exclusive purpose of funding health and welfare benefits for retirees and dependents of the Department 1. The Sub-Trust 2 will be used for the sole and exclusive purpose of funding health and welfare benefits for retirees and dependents of the Department 2. The Trust was formed by the City on Date 1, and it is effective as of Date 2.

The Trust's assets will be used for the sole and exclusive purpose of providing health and welfare benefits to eligible retirees and dependents and to pay reasonable expenses of administering the Trust and the health plans. None of the Trust's assets will be used for, or diverted to, any other purpose. Contributions to the Trust will consist of amounts determined pursuant to the Municipal Code and applicable collective bargaining agreements.

The trustees of the Trust consist of the members of the Retirement Board, a nine-member board appointed by the City Council. The trustees serve for four-year terms and have agreed to perform the duties of the trustees as prescribed in the Municipal Code. The trustees have the exclusive authority and control over the administration and management of the Trust, the investment of the Trust's assets, and the distributions from the Trust.

The Trust is irrevocable and has perpetual existence unless it is dissolved by the City. The Municipal Code provides that upon any such dissolution, and only after paying or making reasonable provision for the payment of all liabilities of the Trust, the trustees will distribute the remaining Trust assets to the City. The distribution will be for the sole purpose of assisting the City in the payment of health and welfare benefits to eligible retirees and dependents. Upon termination or dissolution of the Trust, no assets shall be distributed to, or revert to, any entity that is not either the State, a political subdivision of the State, or an entity whose income is excludable from gross income under IRC § 115.

## LAW AND ANALYSIS

IRC § 115(1) provides that gross income does not include income derived from any public utility or the exercise of any essential governmental function and accruing to a state or any political subdivision thereof.

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that income generated by an investment fund that is established by a state to hold revenues in excess of the amounts needed to meet current expenses is excludable from gross income under IRC § 115(1), because such investment constitutes an essential governmental function. The ruling explains that the statutory exclusion is intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of an entity

engaged in the operation of a public utility or the performance of some governmental function that accrues to either a state or political subdivision of a state. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and that are within the ambit of a sovereign to conduct.

Rev. Rul. 90-74, 1990-2 C.B. 34, holds that the income of an organization formed, funded, and operated by political subdivisions to pool various risks (e.g., casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under IRC § 115(1), because the organization is performing an essential governmental function. In Rev. Rul. 90-74, private interests neither materially participate in the organization nor benefit more than incidentally from the organization.

The Trust was formed to fund the costs of providing health and welfare benefits to retired employees of the City and their dependents. Providing health and welfare benefits to former public employees constitutes the performance of an essential governmental function within the meaning of IRC § 115(1). See Rev. Rul. 77-261 and Rev. Rul. 90-74.

In addition, the income of the Trust accrues to the City. No private interests participate in or benefit from the operation of the Trust, other than incidentally or as providers of goods or services. The Trust's dedication of its corpus and income exclusively for the benefit of the retirees and their dependents satisfies an obligation the City has to provide health and welfare benefits to its retired employees. The benefit to the City's participating employees and their dependents is incidental to the public benefit. See Rev. Rul. 90-74.

Based on the information and representations submitted on behalf of the Trust, we conclude that:

Because the income of the Trust derives from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof, the Trust's income is excludable from gross income under IRC § 115(1).

No opinion is expressed concerning the federal tax consequences under any IRC provision other than the one specifically cited above. In particular, no representation is made that contributions or premiums paid on behalf of or benefits received by employees, former employees, retirees, spouses, dependents, or others will be tax-free. This ruling concerns only the federal tax treatment of the Trust's income, and it may not be cited or relied upon as to any matter relating to the taxation of accident or health contributions or benefits.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. IRC § 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for ruling, it is subject to verification on examination.

Sincerely,

Kenneth M. Griffin  
Chief, Exempt Organizations Branch  
(Tax Exempt & Government Entities)

Enclosure (1)